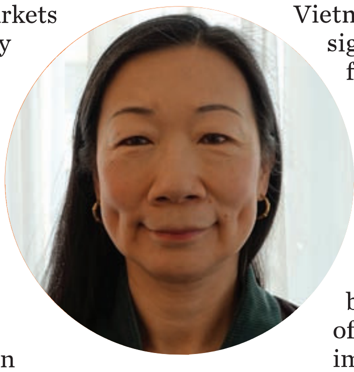
Defying the volatile world

Why Vietnam deserves a place in a diversified investment portfolio

In a volatile and challenging world, many markets remain deeply troubled. Vietnam is arguably a gleaming exception. Its economy and markets continue to provide fertile ground for the value investor.

Vietnam has historically defied the trends of both emerging and developed markets around the world. Its real GDP continued to grow at over 5% per year as the rest of the world collapsed in the US-originated financial crisis of 2008-10. Similarly, the recent China-triggered setback in most of the emerging world has coincided with improving economic growth in Vietnam in the range of 5-7%.

It would be reasonable for a global equity investor to assume that Vietnam is firmly hitched to the Chinese wagon. After all, their political systems are broadly matching. They share state-dominated banking sectors, and both have pursued an export-led manufacturing growth model. Fortunately, this is not the case.



Min Kupfer
chairperson of VietNam Holding

STANDING TALL

Vietnam has an overall balanced trade flow with the rest of the world, but a massive trade deficit with China itself. Moreover, its exports to China are mostly consumer and agricultural commodities that are unlikely to suffer as China decelerates. This stands in marked contrast to countries like Indonesia, Australia, South Korea and Japan, which have much more to lose from a sustained Chinese manufacturing stagnation due to their many industrial, commodity, and supply-chain links.

Further reassurance to investors is the fact that Vietnam and China are at vastly different stages of economic development. China's GDP per capita is some four to five times higher, its manufacturing base is vastly larger, and its costs are higher.

Vietnam's 'catch-up' still has many years to go. It has already profited as an attractive manufacturing location for global businesses, successfully avoiding the common emerging market trap of remaining wedded to its commodity sectors.

The presence of leading global manufacturers is progressively spawning a locally owned array of supporting businesses. The proportion of domestically supplied content in exports has grown by nearly half over the last five years, from 22% to 32%. China at 65% and Indonesia at 40% are indicative of the likely future growth for Vietnam.

MARCHING ONWARDS

While the problems of China and other emerging countries will not be good for the world economy for some time to come, Vietnam stands out as a market that will be able to march to its own beat. This has already been seen in stock market performance comparisons over the past five years.

The US dollar equivalent performance of the VNAS, Vietnam's most representative stock index, has significantly beaten the MSCI emerging and frontier market indices. The cumulative outperformance by Vietnam of more than 30% over the past five years stands a good chance of running for the foreseeable future. Average earnings per share are on the rise, and valuations are modest at less than 12 times earnings.

Continuous privatisation of state-owned businesses – which still produce about a quarter of GDP – is an ongoing long-term project. And importantly, limits on foreign ownership of listed companies – 49% in most cases and 30% for banks – are gradually being increased.

There are many examples of attractive Vietnamese listed companies to invest in. Hoa Phat Group is Vietnam's number one steel producer, founded and led by one of the country's leading self-made entrepreneurs. It has a record of continuous market share gains in the ever growing Vietnamese steel market and is very cost competitive against Chinese imports.

Traphaco is Vietnam's leading herbal medicine firm, boasting one of the country's best earnings per share growth records. Fecon is a leading contractor that specialises in engineering foundation construction.

The three firms, all in the portfolio of **VietNam Holding (VNH)**, an investment fund dedicated to sustainable investments in Vietnam's stock market, trade at between six and 12 times current earnings.

Several Vietnam country funds quoted on either the AIM market or the main London market trade at a discount to net asset value of 15% and more and thus provide an attractive way to access this exciting market. Over the last five years to 31 March 2016, VietNam Holding has outperformed its closest peer by over 40%, and the benchmark index VNAS by over 80%.